United States v. Dalton, Case No. SACV 21-140 JVS (KESx)

Tentative Minute Order re Motions *in Limine* and Related Motions[1]

The United States ("Government) and John C. Dalton IV, *et al.* (collectively "Daltons") move the Court for relief by way of Motions *in Limine* and Daubert Motions. The Court now enters its rulings.

I. Government's Motions *in Limine.*

A. Motion *in Limine* No. 1: Enforce Stipulation.

The Government seeks an order to exclude advice of counsel evidence based upon a stipulation which the Daltons entered into. (Docket No. 111.) The Daltons have filed an opposition (Docket No. 125), and the Government has replied (Docket No. 132).

1. Background.

Underlying this tax dispute are a number of transactions the Daltons entered into. They were represented by counsel. To simplify document production and other issues, the parties entered into a stipulation removing the issue of advice of counsel from the case. (Stipulation, Docket No. 76.) The parties agreed in part:

> Defendants each represent that they are not relying on advice of counsel as part of their defense to any part of this suit and will not offer testimony or other evidence at trial (through Defendants or any of their current or former representatives) of reliance on advice of counsel. To resolve the parties' dispute regarding Defendants' attorney-client privilege claims referenced in paragraph 3 above, Defendants confirm that their agreement that they are not relying on, and thus that they will not introduce evidence of, any advice of counsel includes any "approval" by counsel, whether explicit or

[1]By separate order, the Court has addressed the parties' Daubert motions. (See Docket No. 114, 115, 119.)

implicit.

(Id., ¶ 4; emphasis supplied.)

The parties also agreed on subject matter which would survive the waiver of the advice of counsel defense:

> The parties agree that this stipulation does not impair or limit Defendants'ability to rely on the other facts and documents produced in this matter including their responses to Interrogatory No. 4, specifically, Defendants and their representatives' communications, negotiations, due diligence and related work or interactions with Bryan Cave LLP/PCRG/CDD Holdings, LLC identified in the responses to Interrogatory No. 4, not the "approval" of Defendants' own attorneys identified in their responses to Interrogatories Nos. 1 and 2.

(Id., ¶ 5.)

There is no dispute that the parties' stipulation is binding. The dispute is over the scope of the Stipulation.

2. Discussion.

The Government contends that the Daltons are attempting to evade the Stipulation through the testimony of their expert John O'Donnell ("O'Donnell") and potentially through their own testimony at trial.

The Government cites three passages from O'Donnell. The Court considers each.

> Dr. Blouin, without merit, asserts that this transaction should have raised red flags that the Defendants should have seen. There were no red flags. She further fails to consider that the Defendants employed and relied on seasoned legal and financial professionals who were aware of all pertinent details regarding the transaction, addressed due diligence and conducted negotiations, resulting in the final agreed

> terms of the SPA transaction, which were valid. The experienced professionals retained for this transaction did not identify any red flags to the Daltons.

(Ex. 84, pp. 5-6; emphasis) O'Connell's reference to "seasoned legal . . . professionals" is clearly prescribed by the Stipulation. Use of the term "red flags" is well within the scope of legal advice. Shenwick v. Twitter, Inc., 20221 WL 1232451 at *4 (N.D. Cal. Mar. 2021). This portion of the paragraph is stricken. The balance is within the Stipulation's savings clause.

> The law firm Bohm, Matsen, Kegel & Aguilera, LLP (the "Matsen Firm") were retained by the Daltons and DWC to assist in responding to Buyer's due diligence and other legal assistance relating to the negotiation and terms of the SPA. I have reviewed biographical material from 2006 for Jeffrey Matsen, the lead attorney involved in the SPA, which confirms that he was experienced and well-regarded including in the areas of corporate transactions and tax matters.

(Ex. 84, p. 16.) This passage would appear to be unobjectionable given the Government's concession that "the Daltons may testify that they hired lawyers." (Reply, p. 2.)

> I note the above described independent and well-respected professionals for this stock sale transaction did not indicate that anything was problematic or raised "red flags." In my experience, it is common for parties to rely on their professionals for guidance in transactions such as this. In my opinion, it was reasonable for the Daltons to rely upon their professionals to identify any red flags. This is why parties retain professionals and the fact that the professionals did not raise any red flags gave further assurance to the Daltons that the transaction was valid.

(Id., p. 17.) This passage does not specifically refer to lawyers but a jury could well infer that lawyers are among the "independent and well respected professionals." When referring to professionals, O'Connell shall refer to the firms specifically by name and specialty.

The Government suggests that the Daltons may attempt to testify to reliance on advice of counsel. Such testimony is proscribed, whether it is couched as outright reliance, failure of the lawyers to identify "red flags," "review or vetting," or in any other form. If counsel have a concern that a particular phraseology of a question may run afoul of this ruling, counsel shall bring the matter to the Court's attention before examining.

3. The Motion is granted.

B. Motion *in Limine* No. 2: IRS Internal Analyses.

The Government seeks an order to exclude of IRS employees' deliberations, analyses, and opinions as part of the IRS administrative investigation of the underlying cases. (Docket No. 112.) The Daltons have filed an opposition (Docket No. 126), and the Government has replied (Docket No. 134).

The discovery dispute with regard to the relevance of internal IRS investigative activities is presented again to this Court by way of Motion *in Limine*. The Magistrate Judge held on a motion to compel that the defendants could not overcome the deliberative privilege. (Docket No. 100, pp. 8-9.) The Court agrees.

The trial is *de novo* at which the jury will be asked to find the facts. Oliver v. United States, 921 F.2d 916, 920 (9th Cir. 1990). The internal workings of the IRS are not relevant to the dispute before the Court. Rogers v. United States, 2016 WL 11503067, at *2 (C.D. Cal. Dec. 19, 2016).

The focus of this case is the operative facts behind the 2006 transfers which the Government challenges and the assessment of those facts under California's fraudulent transfer statutes. Cal. Civ. Code §§ 3439.04, 3904.05. The Government's activities long after are not relevant. (Fed. R. Evid. 402.)

The Daltons claim that evidence may be relevant of the issue of waiver. Court granted summary judgment on the Government motion directed to the waiver defense.

The Motion is granted.

C. Motion *in Limine* No. 3: Contract Interpretations.

The Government seeks an order to exclude evidence of contract interpretation which contradicts the plain meaning of the contract. (Docket No. 113.) The Daltons have filed an opposition (Docket No. 127), and the Government has replied (Docket No. 135).

1. Legal Standard.

At issue here is the application of the parole evidence rule. The rule bars claims seeking to vary the terms of a written contract. Riverisland Cold Storage, Inc. v. Fresno Madera Prod. Credit Assn., 55 Cal. 4th 1169, 1174 (2013). The "the principle that when the parties put all the terms of their agreement in writing, the writing itself becomes the agreement. The written terms supersede statements made during the negotiations. Extrinsic evidence of the agreement's terms is thus irrelevant, and cannot be relied upon." (Id.)

2. Discussion.

The dispute here centers on a non-compete agreement which Dalton West Coast, Inc. ("Dalton West") entered into as part of the sale of the business to Cintas Document Management. (Motion, Ex. 8.) The relevant language is in paragraph 1:

> 1. Non-Competition and Non-Disclosure Covenants. The Company and each Operator agree, in consideration for Cintas entering into the Purchase Agreement and the payments to the Company as set forth in the Purchase Agreement and the payments directly to each Operator as provided for in Section 2 herein:
>
> (a) That, for a period of five (5) years from the date hereof, each Operator and the Company will not, either directly or through any other person, firm, corporation or other entity, engage in the Business, on site or off site, which includes the shredding and

> destruction of non-paper items in certain circumstances, as an owner, shareholder, agent or partner, or, in the case of any Operator, serve in an executive position or as an employee with any business which owns or operates a mobile (on-site) or facility based (off-site) paper shredding business or which otherwise conducts paper shredding or product destruction services anywhere within a One Hundred mile radius of the Company's existing locations in Anaheim, California, San Diego, California, San Jose, California and Sacramento, California;

The Court finds that the first sentence is a clear and unambiguous prohibition against competition for the five-year period. The second sentence modifies the limitation to prohibit certain activities of the Operator within a 100 mile radius. That has no effect on the five-year ban anywhere regardless of radiance distance. The language is not reasonably susceptible to a different interpretation. Brobeck, Phleger & Harrison v. Telex Corp., 602 F.2d 866, 871 (9th Cir. 1979). The Court bars Michael Rountree, O'Connell or any other witness from testifying to the contrary. Riverisland Cold Storage, Inc., 55 Cal. 4th at1174. Moreover, status as an expert is no license to evade the rule. McHugh v. United Serv. Auto. Ass'n, 164 F.3d 451, 454 (9th Cir. 1999).

Evidence contradicting the plain meaning of the contract is not relevant, and clearly more prejudicial that probative. (Fed. R. Evid. 401, 403.)

The Motions is granted.

II. The Daltons' Motions.

A. Motion *in Limine* No. 1: Rountree Loan.

The Daltons seek an order excluding evidence of a loan made to third-party Michael Rountree. (Docket No. 116.) The Government has filed an opposition (Docket No. 121), and the Daltons have replied (Docket No. 135).

For many years, Rountree has served as an outside accountant for the Daltons and their business entities. He has also been designated by the Daltons as non-retained expert.

In 2010, four years after the transactions in issue here, John Dalton IV made a personal loan to Rountree in the amount of $200,000. Rountree makes monthly payments, and the loan is still outstanding with a balance of approximately $175,000.

The Court agree with the Government that the loan is evidence of potential bias, and as such is relevant. The fact that the loan was made after the transactions at issue and prior to the Government's initiation of suit is beside the point, particularly in view of Rountree's ongoing payment obligation and the current loan balance. Evidence of the loan is not more prejudicial than probative.

The Daltons' are mistaken that evidence of bias can be categorized as character evidence under Federal Rule of Evidence 608. (Motion, pp. 3-4.) Nor is the brief line of questions line necessary to establish the loan and its particulars harassing. (Fed. R. Evid. 403.)

The Motion is denied.

B. Motion *in Limine* No. 2: Certain Filings.

The Daltons seek an order excluding evidence of certain Forms 1120--Interest Charge ("DISC filings) filed by DWC, at the time known as Certified Document Destruction Co. (Docket No. 117.) The Government has filed an opposition (Docket No. 123), and the Daltons have replied (Docket No. 137).

DISC filings for the years were made in connection with tax elections made by filing Form 478-As. The Daltons' contend that these filings have no relationship to the 2006 sale in issue here, and are thus not relevant. The Government does not argue to the contrary.

Rather, the Government contends that these filings go to the credibility of Rountree because the Government contends that the firm was not entitled to claim the alternative tax treatment. At deposition, Rountree admitted

that he raised no "red flags," but rather executed his clients' decisions. However, the filings resulted in tax deferral–not tax avoidance. That fact is significant.

The Court agrees that the DISC filings shed minimal light on Rountree's credibility and ability to identify "red hearings." Moreover, such evidence would result in a trial-within-a trial; namely, the propriety of filings in unrelated tax years. (Fed. R. Evid. 403.) The case will present the jury with substantial complexity without this diversion.

The Motions is granted.

C. Motion *in Limine* No. 3: Daltons' Personal Assets.

The Daltons seek an order excluding evidence of their personal assets and net worth. (Docket No. 118.) The Government has filed an opposition (Docket No. 121), and the Daltons have replied (Docket No. 138).

At the outset, it is important to note what the Daltons do not seek to exclude:

> This Motion does not seek to exclude evidence of the amounts that each Dalton received following the March 2006 stock sale or from a prior unrelated asset sale. The Daltons have verified these amounts in their interrogatory responses, and these amounts were identified in their 2006 tax returns (for which the Daltons each paid their personal tax obligations).

(Motion, p. 1.) Implicit are tranfers from DWC to any individual Dalton or any joint Dalton entity related to any of the disputed transactions. The Court agrees that this is the appropriate focus.

However, this does not limit the Government to the Daltons' interrogatory responses. If such information appears in monthly reports, such reports are not excluded, although they may be subject redaction to exclude

irrelevant matter.[2] (See Motion, p. 2.)

The Court excludes evidence going only to the Daltons' net worth or financial condition. Such evidence is irrelevant, and because of the potential to inflame the jury, is also more prejudicial than probative. (Fed. R. Evid. 401, 403.)

With respect to any financial documents that contain mixed relevant and irrelevant financial information, the parties are directed to meet and confer no later than ten days prior to trial concerning appropriate redactions. Any remaining disputes shall be presented to the Court prior to trial.

* * * * * * * * * * * * *

Counsel are ordered to advise the parties and all witnesses of the Court's rulings so that there are no inadvertent violations of this Order.

[2]To the extent that a series of documents is offered show a cumulative relevant transfer, the parties should consider the use of stipulated summaries in lieu of the documents.